CONTROL OF LIVING COSTS

by

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COSTS OF LIVING in the United States have been mounting steadily for a year and a half. The consumer price index compiled by the Bureau of Labor Statistics touched a new high in July for the eleventh consecutive month. The rise began, after three years of relative stability, in March 1956 and has been interrupted since then only by a slight decline in the one month of August 1956. The advance since the spring of 1956 now amounts to a full five per cent.

When the index figures for July were announced on Aug. 23,[1] Senate Majority Leader Lyndon B. Johnson (D-Texas) warned that the mounting cost of living might "well become the dominant issue on the American scene." Democratic National Chairman Paul M. Butler, announcing the appointment on Sept. 12 of an Advisory Committee on Economic Policy, said the high cost of living would be one of the first problems considered by the newly formed group. Butler blamed living cost increases on "the mistaken economic policies and fiscal mismanagement of the Republican administration."

The administration itself made a dramatic anti-inflationary move on Sept. 13. Treasury Secretary Anderson announced the creation that day of a new advisory group of officials headed by President Eisenhower and including Anderson, Federal Reserve Board Chairman William McChesney Martin, Jr., Raymond J. Saulnier, chairman of the President's Council of Economic Advisers, and Gabriel Hauge, the President's special economic assistant. The group is to consult on the "financial aspects" of the upward price movement. Its formation gives the administration's anti-inflation planning top-level prestige and will have the special advantage, observers predict, of bringing the President and the Federal Reserve chairman into contact at frequent intervals.

[1] Index figures for August are due to be released in the last week of September.

Administration spokesmen, while as concerned as Democratic leaders over the continuing rise in living costs, have defended staunchly the monetary and fiscal measures taken to restrain inflationary forces. They can point in support of those measures to certain current developments likely to ease the upward pressure on prices. The First National City Bank of New York noted in its monthly letter for September that "Signs that the boom may be getting a little tired continue to crop up here and there." Purchases of industrial equipment fell off slightly in the second quarter; backlogs of orders for machine tools continued slipping; the market for certain steel products was nearing a balance; demand for non-ferrous metals was still sluggish.[2]

The Home Loan Bank Board reported, Sept. 8, that savings increased more sharply in the first half of 1957 than in any comparable period for a decade. The Department of Commerce and the Securities & Exchange Commission estimated the following day that the annual rate of plant and equipment spending by the country's industries would rise only slightly in the third quarter of 1957 and decline in the fourth quarter. Consumer resistance to higher prices has been apparent for some time in the housing market; so far this year the annual rate of dwelling starts has remained well below the 1.3 million rate attained in 1955.

Chairman Martin of the Board of Governors of the Federal Reserve System acknowledged to the Senate Finance Committee in mid-August that factors such as the foregoing were tending to slow down price increases. He was "inclined to think we are reaching a leveling-out process." But Martin nevertheless insisted that inflation was "the most serious economic problem now facing this country."

Marcus Nadler, consulting economist to the Hanover Bank, pointed out in a study for that institution on *The Menace of Inflation*, published Sept. 10, that continued Federal Reserve adherence to a policy of credit restraint differed from the policy followed in 1953. Then, "as soon as business turned downward, measures were taken to increase the availability of bank credit."

> The problem confronting the nation at present [Nadler said] is whether to permit the forces of inflation to continue at the expense of the purchasing power of the dollar or to use all measures available to halt them at the cost of a decline in business activity accompanied by unemployment.

[2] After 15 reductions since Jan. 1, copper prices steadied in mid-September.

Nadler asserted that, although inflation may be slowed by currently emerging anti-inflationary forces, there will be real danger during the next upswing in business activity. With consumer and government spending on the rise, labor demanding higher wages and shorter hours, and pressure on the Federal Reserve to relax credit policy, creeping inflation might "easily degenerate into galloping inflation."

TRENDS IN WHOLESALE AND CONSUMER PRICES, 1950-57

Wholesale prices, unlike consumer prices, remained fairly stable during the first half of 1957, following a steady rise aggregating 7 per cent since mid-1955. The behavior of wholesale prices earlier this year encouraged many observers to conclude that retail prices also would soon reach a plateau. In July, however, the wholesale price index resumed its advance. Steel prices were increased that month, and freight rate increases were approved by the Interstate Commerce Commission in August. Full impact of the steel and freight rate increases has yet to be reflected in the price indexes. The same is true of anticipated price increases of from $30 to $75 on 1958 model automobiles.

Both of the over-all price indexes compiled by the Bureau of Labor Statistics, the wholesale and the retail, reached in July the highest levels attained since the years 1947-49 became their common base period.[3] Measured against a base of 100, representing an average of the prices prevailing in 1947, 1948, and 1949, the wholesale price index touched 118.1, and the consumer price index 120.8, in July.

The wholesale index rose sharply at the outset of the Korean war in mid-1950 and reached a peak of 117 early in 1951. It then fell off gradually to a level of around 110 at the end of 1952 and remained at that point until a new advance began in the middle of 1955. Meanwhile, however, the index component for farm products moved from a high of about 118 at the beginning of 1951 to a low of 83 in December 1955. At that time the average of industrial prices, which remained close to 114 from 1952 until mid-1955, had reached 120. By July 1957 industrial prices were up to 125.6, but farm prices, though rising, were still under 93.

Average wholesale prices of certain individual commodi-

[3] The wholesale index, formerly based on the year 1926, was shifted to the new base in 1952; the consumer price index was shifted from its former 1935-39 base to 1947-49 in 1953.

ties were even farther below the levels attained by the price leaders. Hides and skins, for example, stood at 59.4 in June, when steel mill products touched 175.6; in other words, the average price of hides and skins was 40 per cent lower than in the base period 1947-49, while that of steel mill products was 75 per cent higher than it was a decade earlier.

INDEXES OF WHOLESALE PRICES
(1947-49=100)

Year	All commodities	Farm products	Processed foods	Industrial products
1939	50.1	36.5	43.3	58.1
1950	103.1	97.5	99.8	105.0
1951	114.8	113.4	111.4	115.9
1952	111.6	107.0	108.8	113.2
1953	110.1	97.0	104.6	114.0
1954	110.3	95.6	105.3	114.5
1955	110.7	89.6	101.7	117.0
1956	114.3	88.4	101.7	122.2
1957: January	116.9	89.3	104.3	125.2
July	118.1	92.7	107.2	125.6

SOURCE: Department of Labor, Bureau of Labor Statistics.

The consumer price index also climbed sharply in 1950, kept rising at a reduced pace in 1951 and 1952, and reached a plateau at about 115 in mid-1953. It remained at that level until the latest rise began in March 1956. Component items, however, have not moved uniformly. The index for food at times has been as much as five points below the all-item index, and the index for apparel has been ten points below the over-all average. Housing, transportation, and medical care, on the other hand, have run well above the over-all index.

INDEXES OF CONSUMER PRICES
(1947-49=100)

Year	All items	Food	Housing	Apparel	Transportation	Medical care
1939	59.4	47.1	76.1	52.5	70.2	72.6
1950	102.8	101.2	106.1	98.1	111.3	106.0
1951	111.0	112.6	112.4	106.9	118.4	111.1
1952	113.5	114.6	114.6	105.8	126.2	117.2
1953	114.4	112.8	117.7	104.8	129.7	121.3
1954	114.8	112.6	119.1	104.3	128.0	125.2
1955	114.5	110.9	120.0	103.7	126.4	128.0
1956	116.2	111.7	121.7	105.5	128.7	132.6
1957: Jan.	118.2	112.8	123.8	106.4	133.6	135.3
July	120.8	117.4	125.5	106.5	135.8	138.4

SOURCE: Department of Labor, Bureau of Labor Statistics.

The consumer price index measures average changes in the prices of some 300 goods and services usually purchased by urban families of wage earners and clerical workers. Weights assigned to each item are based on surveys of typical family expenditures. The last survey, however, was made in 1950; although the weights established then have been adjusted for subsequent price changes, they may no longer accurately reflect the distribution of family spending. "As family incomes increase or decrease, as prices of various items change at different rates, and as new and different kinds of goods and services are made available to consumers, families change their spending patterns."[4]

Despite these reservations, and the fact that such items as income tax payments and life insurance premiums are excluded from the compilations, the consumer price index (in which food, clothing and shelter have a combined weight of 71 per cent) probably represents a close approximation of a cost-of-living index for city workers' families.[5]

Factors Underlying the Upsurge of Price Levels

The consumer index shows that during the past five years the cost of services has advanced more rapidly than the price of goods. The index for all services excluding shelter has risen 40 per cent, while that for all commodities has increased by less than 10 per cent. During the same period the index for durable commodities alone, including appliances, automobiles, and furniture, advanced by only about 5 per cent.[6]

Two developments have contributed to this disparity. As the nation's real income has increased, the total demand for services has expanded more rapidly than either the population or the demand for consumer goods.[7] At the

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[4] Eunice D. James, "Relative Importance of Consumer Price Index Components," *Monthly Labor Review*, May 1957, p. 599. Weights assigned to the broad components of the consumer price index follow: Food, 28.7 per cent; housing, 33.1 per cent; apparel, 9.2 per cent; transportation, 11.2 per cent; medical care, 5.4 per cent; personal care, 2.2 per cent; reading and recreation, 5.1 per cent; other goods and services, 5.1 per cent.

[5] See "Cost of Living," *E.R.R.*, Vol. I 1954, pp. 3-20.

[6] Since 1939, however, the indexes for apparel, for certain services (including household operation and medical care), and for all items have risen by about 100 per cent. The rise in food prices since 1939 amounts to 140 per cent, the rise in rents to about 55 per cent.

[7] Total personal consumption expenditures in 1956 were 38 per cent higher than in 1950. Spending for services was up 55 per cent; for non-durable goods, 33 per cent; and for durable goods, 18 per cent. Population had increased by 13 per cent. Higher prices accounted for part of the increase in spending for services.

same time, gains in productivity (and in gross output in the case of food) have helped to hold down prices of goods, while prices of services in rising demand have, in many cases, reflected little or no improvement in productivity. The average daily rate for hospital care, for example, has moved from $10.04 in 1946 to $24.15 today,[8] largely because there have been few operating economies to offset the substantial increase since the war in hospital personnel costs.

It is generally agreed that rising business outlays touched off the rise in wholesale prices which began in mid-1955. Business expenditures for new plant and equipment jumped from $28.7 billion in 1955 to $35 billion in 1956—a $6.3 billion increase. The effects were considerable, according to former Secretary of the Treasury George M. Humphrey:

> The capital-goods boom which emerged in 1955 was of enormous proportions. Industrial construction contract awards had increased 55 per cent during 1955. The volume of new orders for durable goods jumped 34 per cent. . . . The magnitude of these rapidly mounting demands, concentrated in such a short time span, led to a sharp rise in the price of producers' equipment and in the prices of materials, components and supplies used in durable goods manufacturing. . . . Even in lines of industry where demand was not rising so rapidly, some price increases occurred, as producers passed along at least some of the increased cost of materials.[9]

Sharp increases in government spending added to upward pressures on the price level. Net federal budget expenditures increased from $64.6 billion, in the year ended June 30, 1955, to $66.5 billion in the following year and to $69.3 billion in fiscal 1957. State and local government spending has tripled since 1946. Heavy outlays for schools, highways, and other public works have contributed to the capital-goods boom.

Inflation's Impact on Persons With Fixed Incomes

Price increases have not been a source of special concern to persons whose wages or salaries have kept pace with the rising cost of living. About five million workers are receiving wage increases this year under previously negotiated labor agreements, and escalator clauses tied to the consumer price index protect the real wages of about two-

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[8] S. Bruce Black, chairman of Liberty Mutual Insurance Company, as reported in *New York Times*, Aug. 14, 1957.

[9] Statement submitted to Senate Finance Committee, June 25, 1957.

thirds of this group of employees.[10] Workers covered by United Automobile Workers contracts, for example, received deferred wage increases in 1956 averaging 6c to 7c an hour and a net rise of 6c under a cost-of-living escalator clause.

During 1957, however, production workers on the average have made only small gains in real income, partly because of cutbacks in overtime work. In terms of 1956 prices, average weekly earnings of manufacturing production workers amounted to $80.08 in June 1957, or 89c more than in June 1956 but only 9c above the average for 1956. Retail workers' weekly earnings averaged 3c less in June 1957, in terms of constant purchasing power, than a year earlier.

Many groups in the population have had to cope with rising prices without any increase in income. Retirement and survivorship benefits under the Old-Age and Survivors Insurance program were last increased in 1954. Among the 7.4 million retired persons now receiving benefits, payments average $61 a month for single persons and $106 for couples. Among the 2.6 million survivors of insured persons, widows with two children receive an average of $181 a month.

Many of the 7.7 million employees of federal, state, and local governments feel that they have lost ground. About one million federal employees in the classified service and another 500,000 postal workers have received only one pay raise since 1951—an average increase of 7.5 per cent in 1955. Congress voted before adjourning this year to give another substantial increase, but President Eisenhower vetoed the bills on Sept. 7.[11] So-called blue-collar workers employed by the federal government have fared better, because their compensation is adjusted to match the wages prevailing among non-government workers in similar trades and crafts. The blue-collar employees have won increases aggregating an estimated 25 per cent since 1951.[12]

Teachers at all levels have been victimized by inflation, a fact of prime importance in view of the nation's growing

[10] Lily Mary David and Donald L. Helm, "Deferred Wage Increases in 1957 and Wage Escalator Clauses," *Monthly Labor Review*, January 1957, p. 50.

[11] The President said the proposed increases would have far exceeded living cost increases and contributed to current inflationary influences.

[12] See "Unionization of Public Employees," *E.R.R.*, Vol. II 1957, pp. 505-522.

concern over its intellectual resources for the future. The President's Committee on Education Beyond the High School reported in July:

> Over the last half century and especially since 1940, serious erosion has occurred in the real incomes of American college teachers relative to other professional groups and to wage earners generally. The greatest erosion has been at the highest ranks.
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> To restore teaching to a competitive position in the professional labor market comparable to that which it occupied before World War II would require an average increase in faculty salaries of something like 75 to 80 per cent.

Although increases in the consumer price index in the past 16 months have been smaller than those which occurred immediately after World War II and following outbreak of the Korean war, they pose serious questions. If inflation continues, and if it goes on striking hardest at persons in teaching, the public service, and other white-collar and intellectual pursuits, then careers in those fields will lose more and more of the already limited appeal which they have for qualified men and women.

Debate on Causes of Current Inflation

INFLATION is commonly described as what happens when "too many dollars chase too few goods." That is the situation which existed immediately after World War II when consumers rushed into the market in search of goods which had not been available during the war. Strong demand in the face of relative scarcity, coupled with removal of wartime price controls, sent prices skyrocketing from 1946 to 1948.[13] After a brief downturn in 1949, prices took another leap upward in 1950 and 1951 as defense spending increased and the Korean war set off a wave of scare buying.

The current, third round of postwar inflation, however, has been accompanied in recent months by a noticeable slackening of demand. The Federal Reserve System's index of industrial production (1947-49=100), which reached a record peak of 147 last December, fell off steadily during the first six months of 1957 and stood at 144 in August. Output of primary metals alone dropped from a high of

[13] See "Prices and Politics," *E.R.R.*, Vol. II 1948, pp. 631-648.

148 in September 1956 to 133 in August 1957. Steel production fell without pause from 101.6 per cent of theoretical capacity last October to 78.6 per cent in July but rose to 81 per cent in August.[14] The annual rate of business spending for new plant and equipment, which had jumped $1.7 billion between the first and second quarters of 1956, increased only $440 million in the corresponding period this year.

COST-PUSH THEORY: WAGES AND ADMINISTERED PRICES

Classical economic theory holds that prices rise and fall with demand. The seeming paradox that price levels are now advancing in the face of declining demand has led some economists to speak of a new type of inflation fueled by "cost-pushes" rather than "demand-pulls." However, Federal Reserve Chairman Martin denied before the Senate Finance Committee on Aug. 13 that there was anything new in the current inflation.

> Inflation is a process in which rising costs and prices mutually interact upon each other . . . with a spiral effect. Inflation always has the attributes, therefore, of a cost-push. At the same time, demand must always be sufficient to keep the spiral moving. Otherwise the marking up of prices in one sector of the economy would be offset by a reduction of prices in other sectors.
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> There is much to be said for the view that contractual or other arrangements designed as shelters or hedges from inflation have the effect of quickening its tempo. The 5 per cent rise in the cost of living . . . over the last two years has probably reflected and been reflected in more rapidly rising wage costs because of the prevalence of cost of living clauses in many modern wage contracts. Cost plus contracts tend to have the same quickening effect on the inflationary spiral.
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> The spiral is also, however, a demand spiral. At each point of time in the development of the inflationary spiral, there must be sufficient demand to take the higher-priced goods off the market and thus keep the process moving.

Public attention nevertheless has been focused recently on the cost-push argument. Spokesmen for industry and some economists have taken the position that wage increases not matched by increases in productivity are primarily responsible for rising costs and prices. H. Christian Sonne, chairman of the National Planning Association, addressing the New England Council on Sept. 12, questioned whether anti-inflationary monetary and fiscal policies could be "effective . . . in curbing price rises that originate pri-

[14] Steel output is stated as a percentage of weekly net ton capacity as of Jan. 1 each year, although capacity may be increased during the year.

marily from the cost side of production." Sonne doubted it because "one of the factors that determines the price level, namely the wage, is for all practical purposes fixed." The U.N. Economic Commission for Europe observed in a report on Sept. 8 that "Only by reducing economic activity to unacceptably low levels can general monetary and fiscal policies succeed in eliminating the inflationary tendencies arising out of the efforts of organized pressure groups to increase their money incomes."

Labor spokesmen, disclaiming union responsibility for price inflation, counter with the contention that a desire on the part of businessmen for higher profits causes the upward movement of prices. Both the industry and the labor viewpoints were aired during the summer at hearings on "administered prices" held by the Senate Antitrust and Monopoly subcommittee headed by Sen. Estes Kefauver (D-Tenn.).

Economist Gardiner C. Means, who first introduced the term 20 years ago, told the subcommittee on July 9 that, contrary to popular opinion, most wholesale prices outside the commodity markets and many retail prices do not fluctuate with day-to-day changes in supply and demand. These administered prices, he explained, are set by producers or sellers and kept constant over periods ranging from weeks to years. Moreover, the price-setter enjoys an "area of discretion," for within limits imposed by broad market forces there is a "zone of relative price indifference" in which the seller may select a lower or higher price and make substantially the same amount of total profit. Thus, according to Means:

> By keeping their prices on the low side of the area of discretion, business can retard an inflation arising from too much buying power. Conversely, if there were no excess in buying power, business enterprises could decide to raise their prices within the area of discretion so as to increase their unit profit margins. This could lead to a considerable rise in price level without an initial increase in buying power.

Business spokesmen were quick to reject the concept of administered prices. The First National City Bank called it "an old bogey, conjured up to scare people" during the monopoly investigation of the late 1930s.

> The fact is that, when it comes to identifying "new forces" promoting inflationary pressures, there is more to be said for singling out "administered wages." With the labor unions today

> numbering over 17 million members, as against 3 million a generation ago, holding hundreds of millions of dollars in their treasuries, and exercising . . . concentrated power far beyond anything enjoyed by the largest corporations, here indeed is an element of great importance present in larger measure than ever before.[15]

The administered price vs. administered wage debate took sharper form when the Kefauver subcommittee in August called on officials of the United States Steel Corp. to explain their decision to raise the price of steel. U.S. Steel accounts for about 30 per cent of the American steel industry's ingot capacity, and usually sets the pattern for steel prices as well as wage agreements in the industry.

RELATIONSHIP OF WAGES TO PRICES IN STEEL INDUSTRY

The July price increase was "foreordained," U.S. Steel Chairman Roger M. Blough told the Senate subcommittee, Aug. 8, by the contract negotiated with the United Steelworkers after a five-week strike in the summer of 1956. "On July 1 of this year we faced what our recent total wage-cost history demonstrates was about a 6.5 per cent increase in our total costs per man-hour; and to cover these costs in part, we raised our steel prices by an average of 4 per cent."

Blough and other officials testified that the company's employment costs per man-hour increased 250 per cent between 1940 and 1956, but that the price of finished steel mill products rose only 138 per cent in the same period. Employment costs compounded at the rate of 8.1 per cent a year, while output per man-hour increased at an average rate of only 2.7 per cent a year. Profits after taxes amounted to 9.5 per cent of sales in 1940 and to 8.2 per cent of sales in 1956.

Robert C. Tyson, chairman of U.S. Steel's finance committee, pointed out that average hourly earnings of workers in 22 industry groups surveyed by the Bureau of Labor Statistics showed increases averaging almost 200 per cent between 1940 and 1956.

> This universality and uniformity of employment cost inflation, plus the fact that in consolidated industry employment cost represents three-quarters or more of all costs, explain why costs other

[15] *The First National City Bank Monthly Letter*, August 1957, p. 92. Means acknowledged, July 9, that "Wage rates are themselves a form of administered price and . . . are not closely controlled by market forces." He said that "If they are pushed up farther than productivity can increase, the rise in costs is likely to be reflected in higher prices."

> than employment costs tend to parallel the inflation in employment costs . . .
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> For each dollar that our employment costs increase, our total costs increase over two dollars. Economic arithmetic tells us that the new cost-push inflation can never be terminated until inflation in the biggest and most basic cost—employment cost—is terminated.

Organized labor immediately took issue with the company's position. United Steelworkers President David J. McDonald asserted that steel price increases since 1945 had yielded the industry more than $3 in revenue for each $1 of wage increases. U.S. Steel, he said, could "absorb the cost of the wage increase for the remainder of 1957, reduce steel prices by $6 a ton instead of raising them by that amount, and end 1957 with the greatest net profits after taxes in the history of the corporation." The union's research director, Otis Brubaker, told the Kefauver subcommittee, Aug. 20, that U.S. Steel accumulated profits in the first quarter of 1957 at a rate in excess of 15 per cent of net worth.[16]

An A.F.L.-C.I.O. committee has asserted that the steel industry "pioneered the technique" of raising prices at the time wage increases take effect as a "convenient excuse for obtaining large profit margins" while at the same time placing the blame for price increases on labor.[17] The A.F.L.-C.I.O. Executive Council contended on Aug. 14 that U.S. Steel and other corporations had raised prices "to earn enough profits to finance new investment and expansion."

> This practice forces the consumer to provide "costless capital" for industrial expansion. . . . The consumer never becomes an owner of the new facilities; thus he helps finance the new facility without receiving any dividends. The bonanza all goes to those who already are on the inside and further exaggerates the serious imbalance in the distribution of the fruits of the American economy.[18]

Blough turned down Sen. Kefauver's request, Aug. 16, for a breakdown of all of the cost factors behind the July 1 price increase; he said it would mean giving confidential information to U.S. Steel's competitors. The company had estimated the cost of wage increases which went into effect

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[16] Management and labor disagree on the proper method of stating profits, the former relating it to sales, the latter to net worth.

[17] A.F.L.-C.I.O. Economic Policy Committee, *Economic Trends and Outlook*, July-August, 1957.

[18] Management contends that reinvestment of retained earnings is necessary because depreciation charges allowable for tax purposes are grossly inadequate to meet replacement costs. See "Fast Tax Write-Offs," *E.R.R.*, Vol. II 1957, pp. 585-602.

July 1 at 21c an hour or $3.25 per ton of steel, while the Steelworkers had placed the added cost at 15.5c an hour or $2.54 per ton. Kefauver, noting a substantial gap between either estimate and the price increase of $6 a ton, announced Aug. 28 that his subcommittee would resume hearings in October. "This whole matter of costs and prices requires further investigation," he said.

TENDENCY OF WAGES TO OUTSTRIP PRODUCTIVITY GAINS

A crucial element in the wage-cost-price relationship, according to a recent study by the Bureau of Labor Statistics, is productivity. "It represents the margin within which wage increases can be granted without increasing production costs or curtailing the amount available for other income payments." [19]

From 1947 through 1956, the Bureau found, average hourly earnings of all employees increased by 59 per cent, or by 61 per cent when fringe benefits were included. After adjustment for increases in the consumer price index, real earnings per hour were up 30 per cent and 33 per cent respectively. Over the same period, however, output per employee man-hour increased by only 26 per cent.

> It is important to note, however, that between 1947 and 1952 real product per man-hour increased more than real hourly earnings (excluding supplements). By 1953 real earnings had nearly caught up with the increase in productivity, they remained in line through 1955, and it was not until 1956 that real earnings appeared to have definitely exceeded productivity. Real earnings, including supplements, overtook productivity somewhat earlier and have remained ahead since 1954.[20]

Commissioner of Labor Statistics Ewan Clague told the congressional Joint Economic Committee, Jan. 30, 1957, that productivity in the private non-agricultural economy as a whole showed "practically no increase in 1956." Among possible causes for this situation, Clague cited "the moderate gain in output in 1956, utilization of marginal resources, production adjustments to new equipment, and the large increase in the labor force." Failure of the economy to record the usual productivity gains in 1956, he pointed out, followed two years of "higher than average increases, at least in manufacturing, and is not necessarily an indicator of a new trend."

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[19] Bureau of Labor Statistics, *Productivity, Earnings, Costs and Prices in the Private Nonagricultural Sector of the Economy, 1947-56* (May 29, 1957), p. 4.
[20] *Ibid.*, p. 4.

Attempts to Curb Wage-Price Spiral

THE EISENHOWER ADMINISTRATION has relied heavily upon monetary policy and, to a lesser extent, fiscal policy to control cyclical movements in the domestic economy. The 1953-54 recession was met with tax cuts and an easing of credit through reduction of the Federal Reserve discount rate, a principal tool of monetary policy. When recession gave way to boom, Federal Reserve policy switched to one of restraint. Since April 1955 the discount rate has been raised seven times. The most recent increase, from 3 to 3½ per cent, was announced Aug. 8 shortly after major New York City banks had raised their "prime" rate on loans to commercial borrowers from 4 to 4½ per cent.

Democrats have repeatedly assailed the administration's "tight money" policy as a device to enrich big business at the expense of consumers.[21] This attitude explains why the party's leaders in Congress did not accept President Eisenhower's proposal, advanced in his State-of-the-Union message last Jan. 10, that Congress set up a citizens' commission to study "the nature, performance and adequacy of our financial system." Democrats took the position, as stated by Sen. J. W. Fulbright (D-Ark.), that there was "little in this administration's record to indicate the likelihood that an objective study would be made." It was accordingly arranged to have the Senate Finance Committee make the inquiry.

LIMITS TO EFFICACY OF MONETARY-FISCAL MEASURES.

During extensive questioning, beginning June 18, of retiring Secretary of the Treasury Humphrey, Finance Committee Chairman Harry Flood Byrd (D-Va.) and other Democratic members of the investigating group challenged the effectiveness of the administration's efforts to combat inflation through credit restraints. They pointed to the increased cost to the Treasury of funding the public debt at higher interest rates, thus adding to federal expenditures and the inflationary pressures created by such expenditures. They reiterated charges that the "hard money" policy originally applied by the administration in 1953 had

[21] See "Tight Credit," *E.R.R.*, Vol. I 1957, pp. 3-22.

helped to bring on the 1953-54 recession. Concern was expressed lest the same thing occur again.

Federal Reserve Chairman Martin, testifying on Aug. 13, sought both to defend the necessity of successive increases in the discount rate and to define the limits of monetary policy as an anti-inflationary weapon. Arguing that rising interest rates are "an effect of inflationary pressures, not a cause," and that they do not "add to upward price pressures to any substantial extent," Martin added:

> It is necessary to emphasize that there are many influences, other than monetary policies and interest rates, that affect the volume of consumption, investment, and saving and their relationships. Monetary policies operate directly through the volume of bank credit and bank-created money. The volume of current saving out of income and the uses made of new and outstanding savings have a more important bearing upon the availability of investment funds than bank credit. Interest rates, therefore, are influenced by the relationship between investment demands and the availability of savings, independently of monetary policies.

Monetary policy, Martin suggested, can be effective only if matched by sound fiscal policy respecting taxes and government expenditures. Here, he implied, the administration was not doing its share because "It is clear that the present situation calls both for a larger budgetary surplus than we have had or have in prospect, and a continuance of restraint upon creation of new supplies of money." In the final analysis, he said, the only cure for inflation is to be found in "a moderation of spending, both governmental and private, until the demands for funds are balanced by savings."

PRESIDENT'S PLEAS FOR BUSINESS AND LABOR CAUTION

The same note has been struck on several occasions by President Eisenhower. He said in his State-of-the-Union message last January: "Business in its pricing policies should avoid unnecessary price increases. . . . Increases in wages and other labor benefits . . . must be reasonably related to improvements in productivity. . . . Should we persistently fail to discipline ourselves, eventually there will be increasing pressure on government to redress the failure."

The President repeated the substance of this statement at a press conference on June 26 and added that the government alone could not maintain stability of purchasing

power—"There must be statesmanlike action, both by business and by labor." At another press conference, Sept. 3, Eisenhower acknowledged that inflation is "today our major internal problem." He extended his plea for restraint to all citizens by saying: "I am not advocating a buyers' strike but . . . we should buy selectively and carefully."

REJECTION OF REUTHER PROPOSAL TO CUT AUTO PRICES

The most dramatic response to the President's repeated appeals for exercise of "statesmanship" to curb inflation came from Walter P. Reuther. In letters addressed on Aug. 18 to the "Big Three" of the automobile industry—General Motors, Ford, Chrysler—the president of the United Automobile Workers proposed that they "reduce prices on 1958 models to levels averaging at least $100 below the prices for comparable 1957 models." Reuther offered to give "full consideration to the effect of such reduction" on the financial position of the companies when it came time next spring to negotiate new wage contracts.

Reuther asserted that an average reduction of $100 in the wholesale price of cars would amount to $140 at retail, and that the lower price might well result in sale of an additional million cars to offset "substantially or even wholly the effect of reduced prices on profits." The price cut also would place companies in other industries "under strong public pressure to exercise restraint" in setting prices.

Business writers immediately pointed out that the U.A.W. leader was asking the companies to cut profits at once with no assurance of anything concrete in return. Within a week the three automobile manufacturers rejected the Reuther proposal. They all stated that their pricing policies were not a subject for collective bargaining. General Motors President Harlow Curtice countered with the proposal that the U.A.W. agree to a two-year extension of its contract with G.M. "as a contribution to economic stability." Chrysler President L. L. Colbert and Ford President Henry Ford II both compared Reuther's plan to a hypothetical offer by the auto companies to consider what prices to place on their 1958 models if the union would first agree to an immediate cut in wages. Ford suggested that labor leaders contribute to the fight on inflation by refraining from using "the extraordinary leverage and monopolistic power of today's big industrial union."

Appeals for restraint by the President and others do not appear to have been widely heeded. U.S. Steel announced its decision to raise prices the day after Eisenhower's June 26 request for "statesmanlike action." Chairman Blough, testifying later before the Kefauver subcommittee, asserted that "No one company, no one industry, and no one union can alone stop the march of inflation." Blough recalled that on May 1, 1948, when the consumer price index had risen 14.5 percent in a year, U.S. Steel had announced a price cut averaging \$1.25 a ton. The company hoped thereby to help bring about "an early stabilization or reduction in the cost of living."

> I'm sure you all know what happened. Other unions demanded another big round of wage increases—and got them. Other companies had to raise prices to pay for them. Our costs kept soaring skyward. We might as well have tried to stop an express train with a peashooter. So three months later, we had to rescind our price action, increase the pay of our workers, and try to catch up with the parade that we had fallen so far behind.

Skepticism as to the efficacy of voluntary action in combating inflation is widespread. The Guaranty Trust Co. reported in its September survey that employer resistance to rising labor costs now is low, as is consumer resistance to rising prices. "Currency stability is in peril because the people, in their pursuit of other aims, have rejected the discipline that currency stability requires."

Reluctance to Impose Direct Wage-Price Controls

So far, there has been little talk of resorting to direct wage and price controls. Ever since 1952, when Eisenhower campaigned on a promise to remove the regulations instituted during the war in Korea, he has taken the position that imposition of controls on a free economy in peacetime would subvert the American system of government. He restated that view, Sept. 3, and said that "We are not considering legislative controls." At the same time, the President conceded that "The next step, if this thing got out of hand, would be governmental controls in time of peace," though he thought controls under such conditions meant "the beginning of the end."[22] Observing that a controlled economy would not be "the America we know," Eisenhower had warned last Feb. 6 that price and wage controls would become inevitable "unless there is some

[22] Sen. Joseph C. O'Mahoney (D-Wyo.) called on Sept. 4 for revival of Regulation W—the Federal Reserve's control on instalment credit—because consumers were "mortgaging their futures for things they can't pay for."

wisdom exercised not only in government but throughout the whole economy."

If the inflationary spiral comes to a halt in the next few months, the issue of direct controls will remain dormant. In the opinion of many economists, however, any temporary abatement of the upward price movement will not suffice to stop the long-term inflationary spiral which has been under way since World War II. According to one view, the nation's low birth rate from 1931 to 1945 is the "basic cause of wage inflation."

> The yearly increase in the working population is subnormal and will remain subnormal until the middle '60s. By contrast, the nonworking population is growing exceptionally fast. . . . The number of consumers has been rising disproportionately fast as compared to the natural growth in the number of producers. . . . The very high birth rate since 1946 means that the labor market will be gradually flooded with new entrants from the middle '60s on. The effect of this should be the gradual disappearance of the pressure that causes the present wage inflation. We might even witness the return of chronic unemployment and stagnation at that time.[23]

The idea that the American economy is fated to experience a "creeping inflation" for the indefinite future was rejected by Martin in mid-August as an "unwarranted assumption." The Federal Reserve chairman said that if prices were allowed to rise at the rate of 2 per cent a year, the price level would "double every 35 years and the value of the dollar would be cut in half each generation." He warned in conclusion: "No greater tragedy, short of war, could befall the free world than to have our country surrender to the easy delusion that a little inflation, year after year, is either inevitable or tolerable. For that way lies ultimate economic chaos and incalculable human suffering that would undermine faith in the institutions of free men."

[23] Imrie de Vegh, New York investment counsel, interview in *U.S. News & World Report*, Aug. 16, 1957, p. 115.